Forest Management Subgroup — 8/19/08 Meeting
Issue Summary

<u>Topics discussed 8/19:</u>
- Voluntary Opt-in Proposal
- Measurement and Verification

Voluntary Opt-In Proposal

Purpose
Expand forest sector participation in carbon markets beyond the limited offset opportunity, by incentivizing baseline carbon storage (in return for a commitment not to reduce storage below the baseline without penalty); and expand the influence of the cap-and-trade system beyond the capped sectors by use of allowance auction revenue to secure additional carbon retention and storage.

Overarching Policy Question
Is the revenue source for the voluntary opt-in option likely enough to make this option worth spending time on?

Overarching Technical Question
How should the baseline be set for this option? Should it be primarily a "business as usual" baseline, just as for the offset market, or another approach like base period? What effect will this have on the potential to provide additionality and the ability to sell carbon credits in the offset market? What effect will it have on "gaming" the system to artificially raise an entity's apparent additionality?

Broad Options Discussed for Opt-In
Options may be distinguished by two main criteria: **1)** is the option seen mainly as part of the cap-and-trade system, or is it seen mainly as a parallel "complementary program" to address the state's greenhouse gas reduction goals; and **2)** is carbon storage by landowners primarily induced by the state incentive payment for participation, or also by the opportunity to sell surplus credits above the baseline.

Option A
The opt-in approach is mainly seen as *part of the cap-and-trade system*.

- The baseline would be similar to the baseline for offsets.
- The revenue source would be from auction (by the state or the participant) of emission allowances.
- Incentive payments would be made by the state to participants for binding agreements to maintain or increase carbon stocks on their land (i.e. through active forest management activities).

<u>Sub-Option A1</u>
No selling is allowable for "surplus" carbon credits above the baseline (OR payment would come from additional incentive revenue). If the carbon stock on the participant's land

goes below the agreed baseline for the commitment period, the landowner would make penalty payments to the state.

Sub-Option A2
Participants would be allowed to sell "surplus" carbon credits into the cap-and-trade offset market, if they meet all the normal offset requirements. If a participant has a deficit, the participant would need to purchase allowances on the open market and return them to the state.

Option B
The opt-in approach is mainly seen as *a "complementary program,"* parallel to the cap-and-trade system (linked by the source of revenue for incentive payments).

- The baseline could be more flexible.
- The revenue source would be as in Option A.
- Incentive payments would be made to participants as in Option A.

Sub-Option B1
There would be no additional incentive payment within a commitment period for "surplus" carbon credits above the baseline (BUT the participant's land could be re-enrolled at a higher payment level in a subsequent enrollment period). The landowner would make penalty payments to the state for a carbon deficit as in Option A1.

Sub-Option B2
Participants would be allowed to sell "surplus" carbon credits, either to a bank operated by the state, or to other participants in the forest opt-in program who needed to purchase credits (see below). If a participant has a deficit, the participant would need to make penalty payments to the bank, or purchase surplus credits from other participants in the forest opt-in program.

Questions Applicable to Any Option (although the answer may be different for different options)

Revenue Source
Would revenue come from state auction of allowances, or from sale by participating entities of allowances provided by the state?

Would this revenue be collected one time or periodically?

Revenue Amount
How much revenue is needed to provide incentive payments adequate to secure participation? (cf. New Zealand) How many allowances are required?

Commitment Period
Would the commitment period be perpetual or temporary? If temporary, would it be long-term (100 years; 50 years) or could it be shorter-term (5-10 years)?

(If sale of surplus credits is allowed, as in A2 and B2, and the commitment period is temporary, the credit purchaser would have to understand the credit is for a limited time, and discount accordingly.)

Incentive Payment
How would the amount provided to a participant be determined – state formula ($/Ton, given average Tons/acre, X years)? Reverse auction?

How should payment vary for different commitment period lengths, if allowed?

Are payments one-time up-front, or periodic?

Performance Measurement
What's being committed to, in what units is it (and additionality) measured, and for what spatial and temporal scales?

How are the out-of-forest carbon pools included?

How is leakage treated?

Penalty Payments for carbon deficit or premature opt-out
How would this work for the various options presented above?

Participant definition
Should the system be set up to allow only entity-wide opt-in (as opposed to project-level)?

Other?

Measurement and Verification

Premise
The agreed-upon baseline for offsets (BAU) is complex, and requires strict verification to be credible.

Role of the State
1. What is the appropriate role of the state in measurement and verification?
    a. Standard setting
        i. specifying compliance methodologies
        ii. rulemaking to defining the baseline
    b. Assuring harmonization with other C&T/offset systems
    c. Verification
        i. On-the-ground verification
        ii. Spot checking and/or auditing
    d. Certification and/or oversight of 3rd party verifiers
2. Who should do verification?
    a. state agency or board
    b. 3rd party
    c. 3rd party with state standards and state oversight

Verification program design

3. How should verification be done?
    a. programmatically
    b. based on a project-by-project plan that is made part of a binding agreement
4. What is the proper balance of certainty & credibility versus cost?
5. Is industry reporting under Title V of the Clean Air Act an option for a portion of needed verification?
6. Are there measurement & verification standards already in place in other jurisdictions that can be used in Washington?

Paying for verification

7. How should the public cost of oversight be paid for?